

The Cayman Court re-considers its jurisdiction to wind up exempted limited partnerships

Insights - 05/11/2021

In the recent decision *In the Matter of Padma Fund L.P.* (unreported, 8 October 2021) (*Padma*), Justice Parker found that the Grand Court of the Cayman Islands (**Court**) has no jurisdiction to wind up a Cayman Islands exempted limited partnership (**ELP**) on the basis of a creditors' petition. Instead, the Court found that an unpaid creditor must present a petition against the general partner (**GP**) of the ELP. This represents a considerable departure from prior practice in the Cayman Islands, where creditors have routinely sought the winding up of the ELP itself (and not the GP).

Background

Parallax Capital Management is the sole GP of Padma Fund L.P. (**Partnership**). Arbitration proceedings had arisen in respect of a joint venture involving the Partnership and Atlantic Aurum Investments B.V. (**AAIBV**) and San Miguel Holdings Corp (**SMHC**). AAIBV and SMHC (**Petitioners**) had obtained a costs award against the Partnership in those proceedings which went unpaid.

The Petitioners presented a petition against the Partnership pursuant to section 92(d) of the Companies Act (2021 Revision) (**Companies Act**), on the basis that the Partnership is unable to pay its debts. Section 36(3) of the Exempted Limited Partnership Act (2021 Revision) (**ELP Act**) provides that, in certain circumstances, Part V of the Companies Act (containing the regime for corporate insolvencies) applies to ELPs as if they were companies.

The Partnership, acting by the GP, primarily opposed the Petition and sought its dismissal on the basis that the Court did not have jurisdiction over a creditors' petition presented against an ELP pursuant to section 91 of the Companies Act (**Section 91**); being the section which lists the entities over which the Court has jurisdiction to make a winding up order. [1]

ELPs

An ELP is a Cayman partnership that is registered under the ELP Act and has the following relevant features:

- it has no separate legal personality and cannot own property in its own right;
- all management responsibility (including the entry into contractual or other arrangements) for the ELP is vested in the GP;
- legal proceedings by or against the ELP may be instituted by or against one or more of the GPs only;
- all rights and property of the assets of the ELP are held by the GP on statutory trust as an asset of the ELP; and
- its GP has unlimited liability; in the event that the assets of the ELP are inadequate, the GP will be liable for all debts and obligations owed by the ELP.

Previous position

As noted above, it was previously understood that the Court had jurisdiction to hear and determine creditors' petitions against ELPs, and this was recently confirmed in *In the Matter of XIO Diamond* (unreported, 30 April 2020, FSD 256 of 2019 (IKJ)) (*XIO Diamond*). In *XIO Diamond*, Justice Kawaley considered the Court's jurisdiction to wind up an ELP on just and equitable grounds pursuant to s.92(e) of the Companies Act. In determining that such a jurisdiction did exist, Justice Kawaley relied upon section 36(3) of the ELP Act, which provides as follows:

“Except to the extent that the provisions are not consistent with this Act, and in the event of any inconsistencies, this Act shall prevail, and subject to any express provisions of this Act to the contrary, the provisions of Part V of the Companies Act (2021 Revision) and the Companies Winding Up Rules, 2018 shall apply to the winding up of an exempted limited partnership and for this purpose...”

Given the wording of section 36(3), Justice Kawaley formed the view that, whilst section 36(3) did not provide a freestanding judicial power to make a winding up order against an ELP, it did apply Part V of the Companies Act to the winding up of ELPs such that the Court had the jurisdiction to wind up ELPs, including in respect of creditors' petitions on the grounds of insolvency.

This analysis was challenged by the Partnership.

Decision

Contrary to the analysis in *XIO Diamond*, and specifically rejecting it, Justice Parker found that, on a proper construction of the statutory provisions, section 36(3) of the ELP Act could not have imported the Court's jurisdiction under Part V to make a winding up order against an ELP. In his view, Part V was inconsistent with the ELP Act for the following reasons:

- the statutory scheme imposed by the ELP Act indicates that the GP is the entity via which obligations are enforced against the ELP; [2]
- the entities over which the Court has jurisdiction were clearly delineated in Section 91 and do not include an ELP; and
- there already exists the jurisdiction for an ELP to be wound up and the partnership dissolved under the ELP Act and/or the Partnership Act (2013 Revision) (**Partnership Act**), [3] including on the ground that it is just and equitable to do so. If Part V were to apply, there would be two applicable jurisdictions via which a partner could petition for a winding up of an ELP on that ground. Justice Parker considered that the addition of this second, redundant jurisdiction could not have been the intention of the legislature.

Justice Parker therefore held that the appropriate course was for a creditor to present a petition against the GP. In his view the only role for Part V in the winding up of an ELP was after the commencement of the liquidation [4] to provide a scheme for the orderly winding up of the ELP's affairs. He noted that, once appointed over the GP, the official liquidators will hold the assets of the ELP on statutory trust to be realised and distributed in accordance with Part V. In the event of a shortfall in the ELP's assets, the official liquidators would then have a claim against the separate assets (if any) of the GP and such claim would constitute an unsecured claim in any liquidation of the GP.

Conclusion

If the analysis in *Padma* remains unchallenged, it now appears necessary for a creditor of an ELP with an unpaid debt to present a petition against, not the ELP itself, but its GP, in order for official liquidators to be appointed. This disapplication of Part V, in some respects, may be seen as simply a change in form over substance. [5]

However, there are a number of matters which arise as a result of the decision which, in due course, will need to be clarified. The most obvious example is that there are now (at least) two tests for insolvency which would appear to be relevant when winding up an ELP: the test for ELPs provided for in section 2 of the ELP Act, [6] as well as the test for corporate entities in section 92(d) of the Companies Act, which would be relevant to winding up the GP should the ELP itself have insufficient assets to satisfy the claims of its creditors (whether that GP is a Cayman company or a foreign company such as a Delaware LLC). It is unclear from the judgment how those tests will interact and be applied and the relevant circumstances which the Court must consider when doing so.

More fundamentally, aside from the uncertainties arising from the decision, there is an open question as to whether the Court in *Padma* has come to the correct conclusion. Not only is it contrary to previous authority, but it would also seem to be contrary to the apparent legislative intent behind section 36(3) of the ELP Act, namely to ensure that the same statutory scheme for winding up was to be applied to both companies and ELPs. [7]

Given *Padma's* departure from the position as it has been understood in the jurisdiction for some time, a position which has been supported by recent authority, it is likely that the Cayman Islands Court of Appeal will be asked to provide judicial clarity on the position in due course. In light of the importance and prevalence of ELPs as investment vehicles, such clarification would be welcomed. In the interim, we are closely monitoring these developments and considering its implications for investment fund vehicles.

[1] If the Partnership succeeded on that ground then the other grounds became irrelevant as the Court would have no alternative but to dismiss the petition.

[2] In particular, Justice Parker relied upon section 33(1) of the ELP Act which provides that legal proceedings by or against the ELP may be instituted by or against one or more of the general partners only.

[3] Which applies by virtue of section 3 of the ELP Act.

[4] Whether pursuant to the provisions of the Partnership and ELP Act or by successfully winding up its GP.

[5] This is particularly so with respect to the Court's jurisdiction to wind up ELPs on just and equitable grounds. A limited partner will still be able to present the petition against the ELP on this ground but instead reliant on section 35 of the Partnership Act.

[6] Pursuant to section 2 of the ELP Act, the ELP is deemed to be insolvent when the GP is unable to pay the debts and obligations of the ELP in the ordinary course of business as they fall due out of the assets of the ELP, without recourse to the separate assets of the GP not contributed or committed to the ELP.

[7] See, for example, section 36(3)(a) of the ELP Act which provides that references in Part V to a company shall include references to an ELP. Where section 91 of the Companies Act lists a company as an entity the Court has jurisdiction to wind up, the judgment fails to explain why, despite section 36(3)(a) of the ELP Act, a company should not include an ELP in this context.

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